DEPARTMENT OF JUSTICE

Statement by

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Before the
Subcommittee on Postal Service
House Government Reform Committee

on
H.R. 22, “The Postal Modernization Act of 1999"

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I am pleased to be here this morning to present the views of the Antitrust Division on H.R. 22, the Postal Modernization Act of 1999. My written statement and remarks here this morning present the views of the Antitrust Division and do not purport to address issues outside of our areas of expertise. Therefore, the Division's comments should not be read as reflecting the position of the Department of Justice or the Administration with respect to overall postal reform. At the outset, I would like to provide a brief overview of the antitrust laws of the United States and then turn to thoughts about the Postal Service and some thoughts about H.R. 22.

THE ANTITRUST LAWS OF THE UNITED STATES

I would like to start by discussing the purpose and scope of the antitrust laws. For over a century, the United States has committed itself to protecting free and unfettered competition in the vast majority of markets in the economy. The Sherman Act, passed in 1890, has been called the Magna Carta of free enterprise. In general, the United States operates a free-market economy subject to the antitrust laws. Time and again, relying on free-market competition has allowed consumers numerous benefits, including more innovation, more choice and lower prices than that of economies where free competition has been limited.

The main provisions of the Sherman Act are Section 1 and Section 2 of the Act, and they are, in conjunction with Section 7 of the Clayton Act, the primary antitrust enforcement tools. Section 1 of the Sherman Act prohibits contracts and conspiracies in restraint of trade. Section 2 of the Sherman Act prohibits monopolization or attempts to monopolize. Section 7 of the Clayton Act prohibits mergers or acquisitions that may tend to substantially lessen competition. Let me spend just a little more time on the types of activity that may violate these sections of the antitrust laws.

Collusion, which means that firms are agreeing with each other to restrain competition among themselves, is a violation of section 1 of the Sherman Act. It virtually always results directly in inflated prices to consumers and denial of choices in the marketplace; indeed, that is its purpose. The most common of these agreements are agreements to fix prices, agreements to allocate markets, and agreements to boycott particular customers, suppliers, or competitors. Price fixing includes not only agreeing on the specific price, but also agreeing to increase or depress price levels, or agreeing to follow a formula that has the intended effect of raising or depressing prices or price levels. Allocation of markets includes not only agreeing to divide up geographic areas to avoid competition, but also agreeing to divide up customers or suppliers within an area, or agreeing to divide up a sequence of bids. Group boycotts include any agreement among competitors that they will deal with their customers or their suppliers only on particular terms.

A second type of antitrust violation is monopolization or attempting to monopolize, which violates section 2 of the Sherman Act. Under section 2, it is not necessary to prove an agreement. One firm can illegally monopolize by itself. But section 2 monopolization cannot be proved just by showing that a firm has engaged in restrictive conduct. The law also requires proof that the firm has a monopoly and that it engaged in the restrictive conduct in order to acquire or maintain the monopoly. Or, in the case of attempted monopolization, it must be

proved that the firm stands a "dangerous probability" of obtaining a monopoly as a result of the restrictive conduct. To prove "dangerous probability," the courts generally require, for starters, that the firm involved in the restrictive conduct already has a quite large market share. And even a large market share might not be enough, if other facts indicate that the restrictive conduct is unlikely to succeed in creating a monopoly.

In addition to prohibiting anticompetitive collusion and monopolization, the antitrust laws also prohibit anticompetitive mergers and acquisitions. A merger or acquisition that may substantially lessen competition in a product market and geographic market violates section 7 of the Clayton Act. Under Clayton Act merger review, the principal focus is whether the merger would change the incentives and ability of competitors to such a degree that competition would be substantially lessened. The remedy for a merger that violates the Clayton Act typically is to sue to stop the merger, or to insist that it be modified to remove the cause for antitrust concern.

The Division analyzes mergers pursuant to Horizontal Merger Guidelines developed jointly by the Department of Justice and the Federal Trade Commission (the Antitrust Division shares civil antitrust enforcement responsibility with the Federal Trade Commission). The analysis is aimed at determining whether the merger is likely to create or enhance market power, or to facilitate the exercise of market power, in any relevant market. Market power is the ability of a firm or group of firms to raise the price they charge to customers -- or to lower the price they pay to suppliers -- a small but significant amount without being defeated by competitive responses by other competing firms.

PAST JUSTICE DEPARTMENT VIEWS ON POSTAL ISSUES

Since the enactment of the Postal Reorganization Act of 1970, the Department has engaged in an active program of competition advocacy with respect to postal issues. In appearances before the Rate Commission and in various Executive Branch communications, the Department has challenged efforts by the Postal Service to expand the scope of the protections afforded under the Private Express Statutes. We have suggested the need for a comprehensive review of competition in domestic and international markets for mail services, noting the USPS's expansion into competitive markets and the many ambiguities surrounding its legal status under the Private Express Statutes. These are some of the issues we have addressed:

- In 1977 the Department of Justice issued a report on the Private Express Statutes which examined the basis of the postal monopoly and suggested competitive alternatives.

- In 1979 the Antitrust Division submitted comments to the Postal Service on the competitive impact of its regulations and urged the repeal of regulations treating "data processing materials" as within the scope of the term "letter" as used to delineate the scope of the postal monopoly.

- In 1986 the Antitrust Division prepared comments urging the USPS to suspend or limit its International Priority Airmail Service pending development of a factual record adequate to ensure against anticompetitive cross-subsidization; in a separate proceeding the Antitrust Division urged the USPS to reject proposed rules that would restrict the ability of remail services to compete for international mail traffic.

- In 1988 the Antitrust Division submitted comments critical of the USPS proposal for modifications to the terminal dues system for delivery of international mail.

- In 1991 the Antitrust Division reiterated its opposition to the USPS proposal for modifications to the terminal dues system.

- Most recently, the Department of Justice prepared written comments in response to Chairman McHugh's request for views on the antitrust and competition policy provisions in H.R. 22. Our August 1998 letter continues to have general application to H.R. 22, notwithstanding modifications that may have been made to the bill currently under consideration.

Last year we also took an active role in urging support for a legislative amendment transferring responsibility for international postal policy from the USPS to the State Department. The President signed the measure into law, thus formalizing the end of the USPS' direct representation of US interests at meetings of the Universal Postal Union, the international standards-setting body.

The Department's position has not wavered on key competition policy issues affecting domestic and international mail. In the years since the reorganization of the United States Post Office, we have been critics of attempts by the USPS to use its regulatory authority to expand the scope of the statutory protections afforded by the Private Express Statutes, and we have opposed efforts to erect restrictions on competition in international mail services.

Furthermore, the Department takes the firm position that statutory exceptions to the federal antitrust laws should be avoided whenever possible. Federal competition policy objectives are best served when the federal antitrust laws are applied uniformly, rather than allowing them to be distorted to give special protections to certain classes of competitors or to selected industries or economic sectors. We believe that Congress should create exceptions to the antitrust laws only in the exceedingly rare instances when the government's strong interest in preserving competition is outweighed by a compelling and irreconcilable social policy objective, and that even in those rare instances the exception should be as narrowly drawn as possible.

THE PROPOSED LEGISLATION

Until recently, there has not been serious legislative focus on possible modernization of the United States Postal Service since the enactment of the Postal Service Modernization Act of 1970. Given that almost three decades have passed, with accompanying technological and other changes, it is not surprising that thought would again be given to whether changes to the regulatory system in which the Postal Service operates are appropriate.

In broad overview, the Postal Service now engages in a number of activities which can be considered competitive. For example, there are a number of options for people to send material to a recipient quickly (that is within 1 or 2 days), typically referred to as express mail. At the same time, it appears unlikely that other entities currently possess the infrastructure necessary to compete for general first-class mail delivery at the size and scope necessary to preserve universal service of mail delivery.

Given these competing observations, the question for policy makers is whether an acceptable system can be devised to put the Postal Service on roughly the same footing as other competitors in those areas in which it faces competition. Such a system should ensure that the Postal Service has neither inherent advantages nor disadvantages over other competitors, while ensuring that the Postal Service has the ability to efficiently meet the requirements of the universal service obligation and provide the service for which they do not face competition.

This legislation recognizes that certain of the activities currently engaged in by the Postal Service, such as express mail, are subject to competition. Other services, such as regular first-class mail, retain an important universal service policy dimension and are not subject to full competition at this point in time. The legislation attempts to deal with this dichotomy by treating the competitive and monopoly services differently.

Under the legislation, price regulation on competitive products is limited substantially, requiring only that the prices established by the Postal Service cover the direct and indirect postal costs attributable to such products. Competitive products collectively must bear at least an equal proportional mark-up for institutional costs as do all non-competitive and competitive products combined. The rationale behind such a requirement -- that the Postal Service should not be allowed to subsidize its competitive activities by loading up its overhead costs in the non-competitive category of products, for which it earns a guaranteed return -- is a legitimate competitive concern of cross-subsidization. At the same time, the intent of the legislation is that as long as the cross-subsidization is avoided, the Postal Service will have the same freedom to price its competitive goods and services as its competitors. An important corollary to this structure is that the intent of the legislation is to subject the Postal Service to the antitrust laws for activities related to non-monopoly products.

This structure seems to place the Postal Service closer to equal footing with its competitors with respect to competitive products. It allows greater flexibility to the Postal Service while, at the same time, subjecting it to the same antitrust laws that its competitors face. It provides more pricing flexibility to the Postal Service while attempting to ensure that

inappropriate subsidization does not occur. Of course, one of the keys in implementing such a regulatory pricing system will be to ensure that direct and indirect costs are appropriately taken into account.

With respect to services for which the Postal Service remains a monopoly provider, the legislation revises the price regulation method, going from a cost-based system to a price-cap regulatory system. In general, price-cap regulation tends to have advantages over a pure cost-based system in many instances. The prime concern with a cost-based system is that the incentives for cost control are seriously lacking and often inefficiency prevails. In a price-cap system, on the other hand, there is more of an incentive for attempting to lower the cost of the provision of the regulated services, since cost savings can be retained by the entity subject to the price-cap regulation. At the same time, since the mere increase in costs would not subject rates to increases, there is likely to be less of an incentive to attempt to misallocate costs from the competitive services to the monopoly services.

I would like to turn now to comments on two specific provisions of the legislation, section 305, "Unfair Competition Prohibited" and section 603, "Equal Application of Law to Competitive Products." Section 305 appears to create a regulatory regime pursuant to which the Postal Regulatory Commission would prescribe regulations to enforce statutory requirements that the Postal Service not, among other things, create any competitive advantage for itself through regulation or any agreement. We would like to discuss this section with the subcommittee. We are somewhat concerned that the standards contained in this section appear to diverge from the antitrust laws, and about the availability of different forums for addressing the same conduct. It could be possible that legitimate and procompetitive business practices may be inhibited by this section. It may be that our concerns can be resolved by additonal discussion.

Section 603 would require the Department of Justice to prepare a comprehensive report identifying Federal and State laws that apply differently to products of the Postal Service in the competitive category of mail and similar products provided by private companies. The Department of Justice is not an appropriate agency for such an assignment. We are a law enforcement agency and have neither the resources nor the expertise with State law to conduct such a study. We are concerned such a requirement would require resources to be taken from antitrust law enforcement and therefore detract from the appropriate enforcement of the antitrust laws. We respectfully request that if this reporting requirement is retained as the legislation goes forward, the job be assigned to a more appropriate agency.

CONCLUSION

Competition principles are at the core of the American economy and should be maximized to the fullest extent possible in reform legislation. We look forward to continuing to work with the Subcommittee on the important issue of postal reform.